MONTANA MONEY SCHOOL

State Auditor John Morrison

Savings and Investing

It is possible for money to work for you in two significant ways — savings and investments. Many people think saving and investing are the same thing, but there is a world of difference. Well-informed people know how to make their money grow by balancing risk and return when they make saving and investing decisions.

SAVINGS

Savings is income withheld from current spending for future use. "Pay Yourself First" is the initial step to saving money. Make paying yourself first a regular part of your savings and investing goals. This money management principal is a lifetime tool that makes it possible to reach short- and long-term goals. Include the "PYF" plan in your budget and save one dime for every dollar you earn.

Money deposited into a savings account usually is very safe, but has a lower interest rate. The interest rate is quoted as a percentage and represents how much the bank will pay the account holder for the deposit. (e.g., if the annual interest rate is 5 percent, an account with $100 will receive approximately $5 a year.) The savings and interest are federally insured against loss.

Savings are liquid, which means they are easily converted into cash. For this reason, they are an ideal place for funds that will be used for routine purchases and short-term goals.

SAVINGS PRODUCTS

Savings accounts usually are the first banking product people use. Most savings accounts have a relatively low interest rate.

Money-market funds are low-risk mutual funds that invest in stable, short-term securities. These funds usually pay a slightly higher interest rate than a savings account, but less than a certificate of deposit. Savers can take their money out at any time without paying a penalty.

Certificates of Deposit often are referred to as "CDs," which are specialized deposits made at a bank or other financial institution. Savers place their money in the bank for a specified period of time, usually several months or years, and the bank promises to pay a certain rate of return or interest.

INVESTING

To obtain higher earnings, individuals can consider investing. Investments typically earn higher returns than savings accounts, but usually involve more risk. Investments are not insured against risk or loss resulting from changes in financial markets. There is greater volatility (price movement) with uninsured investments so individuals should invest only the amount that they do not need for everyday expenses or for expenses they will have in the near future. Remember – investing is for long-term security, not to get rich quick.

MAJOR TYPES OF INVESTMENTS

Most people use savings accounts to park the money they need to pay monthly bills and to accumulate funds for emergencies and investing. After building their savings, some individuals turn to the financial markets to invest a portion of their money, intending to make it grow faster. Major types of investment categories include the following:

Stocks represent a share of ownership in a company. People who own stock are considered shareholders or stockholders in the company. Investors make money from stock in two ways. The first is through dividends, which are payments to stockholders from the profits of the corporation. The other way is by selling stock when the stock price increases. This is how most people earn money through owning stock. The price of a stock will increase when there are more people who want to buy the stock than there are people who want to sell it.

Mutual Funds allow people to invest in stocks with reduced risk. Investors send their money to a mutual fund company, which pools it with other investors' money and invests it in many different stocks or bonds. This is known as ***diversification,*** which reduces risk because it allows individuals to offset losses in some individual stock with gains in others. Mutual funds are a recommended investment choice for young investors since the risk is lower than investing in individual stocks.

Bonds are like an 'IOU." Corporations and governments sometimes need to borrow money. The bond investor lends them money by buying a bond. The issuer promises to pay the investor back on a certain date, with a set amount of interest. Bonds are known as "fixed-income" securities because the amount of income the bond will generate each year is "fixed" when the bond is sold.

Many investors rely on the advice of a broker or financial planner. These financial professionals must make recommendations that are appropriate for the investor, offer full disclosure of material facts related to the investment and treat the investor fairly. Remember - all investors must be responsible for educating themselves to make informed investment decisions.